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C O N F I D E N T I A L SECTION 01 OF 02 BAGHDAD 002299

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SUBJECT: (C) IRAQ OIL: MINISTRY OFFICIALS SKEPTICAL AS
COURTING CONTINUES

REF: BAGHDAD 2204

Classified By: DCMAT Patricia Haslach for reasons 1.4 (b) & (d)

11. (C) Summary: In advance of the second oil and gas bid round, international oil companies (IOCs) are increasing their engagement with the Ministry of Oil (MOO). While the Government of Iraq (GOI) has yet to determine how it will deal with oil fields that were not awarded in the first bid round, IOCs are hoping to strike deals that will give them access to these fields. At the same time, IOCs are trying to convince the GOI to make the terms for the second bid round more flexible. Oil Minister Shahrastani is meeting with IOCs August 25 in Istanbul to discuss the terms for the second round. In contrast to Shahrastani's optimism about the way forward, several senior MOO officials believe no contracts will be signed with IOCs, including the British Petroleum (BP)/China National Petroleum Corporation (CNPC) consortium and Shell, until after Iraq's national elections in January. They cite ambiguous hydrocarbons laws and tax regulations and archaic business practices as major impediments. End Summary.

Until January Elections, BP/CNPC Contract Unlikely . . .

12. (C) MOO and the BP/CNPC consortium are unlikely to finalize a contract to develop the Rumaila oil field (the only field awarded in Iraq's June 30 oil and gas bid round) until after Iraq's national elections in January, according to several senior MOO officials. The parties continue to negotiate, and -- in a positive development -- the South Oil Company is now involved in the talks. MOO officials have noted reports that BP has sold up to 16 percent of its share of the consortium to its partner CNPC, a move viewed as a possible indication of BP's uneasiness with the deal. (Comment: BP officials have said publicly they expect to conclude a contract before the end of the year. In a debrief in Baghdad on their first round of negotiations, BP reps noted that MOO bureaucrats have frequently raised objections that could slow down the talks but that Shahrastani has consistently overridden them to keep the talks moving forward. We assess that Shahrastani and the GOI want to see a deal signed quickly -- certainly in advance of the second bid round November 30 and the January elections -- and will continue to press ahead despite concerns in the ranks. End Comment.)

. . . Royal Dutch Shell Contract Unlikely

13. (C) MOO's South Oil Company and Royal Dutch Shell are also unlikely to sign a contract for collecting and processing natural gas in Basrah province (instead of flaring the gas,

as Iraq currently does) until after the January elections, senior MOO officials say. Despite nearly a year of negotiations, MOO appears to be struggling to comprehend the seven legal documents Shell presented to codify the deal. (Comment: MOO may be reluctant to sign the contract because it has limited familiarity with modern oil and gas contracts and fears it might grant too many benefits to Shell, increasing the likelihood of the contract becoming an issue in the election campaign. End Comment.)

ExxonMobil Complains, but Pursues Contracts

¶4. (C) In an August 19 meeting with Deputy Chief of Mission for Assistance Transition (DCMAT) Haslach, ExxonMobil's Qfor Assistance Transition (DCMAT) Haslach, ExxonMobil's President for (Western) Upstream Ventures said the GOI rejected ExxonMobil's June bid on the West Qurnah oil field even though it would have generated up to \$50 billion in investment, up to \$600 billion in revenue to the GOI, and up to 200,000 direct and indirect jobs. He said ExxonMobil's bid would have given the GOI a 98 percent share of gross revenue, compared to a global average government share in the "70 percent" range for such oil and gas contracts. The bid failed, he said, because MOO demanded a 99 percent share. This one percent difference, while negligible to the GOI, would have cut ExxonMobil's expected revenue share in half, making the deal impossible. He said ExxonMobil would attempt to "educate" the GOI on standard global oil and gas practices and encouraged the USG to do the same.

¶5. (SBU) Note and Comment: In the June bid round, the

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consortium led by ExxonMobil had the highest bid score of the five bidders for the West Qurnah oil field, but ExxonMobil's bid exceeded the maximum remuneration fee allowed by MOO. When neither ExxonMobil nor any other bidder was willing to lower its fee, the field was not awarded. Bids for seven of the eight fields on offer in June were also rejected by MOO because the IOCs declined to accept the maximum fee allowed by MOO. (ExxonMobil's consortium also had the highest bid score for the Rumaila oil field, but the field was awarded to BP/CNPC, the only bidder that accepted the maximum fee allowed by MOO.) Because Iraq's next bid round consists only of underdeveloped or undeveloped fields (whereas the first round consisted of well-known "national-jewel" oil fields), MOO might be persuaded to allow higher remuneration fees. If MOO does not offer enticing rates of return, the next bid round could fail. End Note and Comment.

¶6. (C) The Exxon official complained that many aspects of MOO's model contract for the June bid round have not been elaborated or finalized, such as taxes and the cost-recovery period. (Comment: Most of these points should be addressed at the August 25 Istanbul meeting with IOCs. End Comment.) He commented that transparency and discretion should not be mutually exclusive when awarding contracts and used Norway and the UK as positive examples. Despite these uncertainties, he said, IOCs want to do business in Iraq because the country's oil potential creates a one-of-a-kind opportunity.

¶7. (C) He added that ExxonMobil will attempt to close contracts from the bids it submitted in the June bid round, participate in the next bid round, and attempt to close (unspecified) contracts outside either bid round. (Comment: If ExxonMobil is successful in this last activity, it could harm the hard-won perception that oil and gas contracts will be transparently awarded. End Comment.) As part of its strategy, ExxonMobil is encouraging the GOI to adopt a comprehensive (upstream and downstream), integrated energy plan and will recommend that the GOI take another look at a "USD 100 billion transformative plan" that ExxonMobil first presented in 2006.

18. (C) Baker Hughes's Iraq Country Director also expressed frustration about entering the Iraq oil sector. He complained that even with MOO's support, Baker Hughes has been unable to register a new company in Iraq due to archaic business practices, and therefore cannot sign a contract with MOO. He said this roadblock has arisen after his firm waited a year for security conditions to improve. Nevertheless, in a separate August 17 meeting, Baker Hughes's Chief Operating Officer told DCMAT Haslach that the firm is already training local employees and laying the groundwork for an office in Basrah.
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